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R2001-0033

March 8, 2001

**Closing Date: Thursday, March 22, 2001**

FROM: Vice President and Secretary

**Second Report on the Implementation of the Prototype Carbon Fund  
and  
Proposed Amendments to the Instrument Establishing the Fund**

1. Attached is a President's Memorandum entitled "Second Report on the Implementation of the Prototype Carbon Fund and Proposed Amendments to the Instrument Establishing the Fund".
2. In the absence of objections (to be communicated to the Vice President and Secretary by the close of business on March 22, 2001), the recommendation contained in paragraph 20 of the Memorandum will be deemed approved and so recorded in the minutes of a subsequent meeting of the Executive Directors.
3. Questions on this document may be referred to Mr. Johnson (X31053) or Mr. Newcombe (X36010).

Distribution:

Executive Directors and Alternates  
President  
Bank Group Senior Management  
Vice Presidents, Bank, IFC and MIGA  
Directors and Department Heads, Bank, IFC and MIGA

FROM: The President

Second Report on the Implementation of the Prototype Carbon Fund  
and  
Proposed Amendments to the Instrument Establishing the Fund

**A. Background**

1. On July 20, 1999, the Executive Directors of the International Bank for Reconstruction and Development (“IBRD”) approved Resolution 99-1 authorizing the establishment of the Prototype Carbon Fund (“PCF”). Management agreed at that time that semi-annual reports on lessons learned by the PCF would be provided to the Executive Directors.

2. This is the second semi-annual report to the Executive Directors.<sup>1</sup> This report has been delayed to March 2001 to accommodate the necessary review and agreement by PCF Participants to two proposed amendments to the PCF Instrument. The proposed amendments would: (1) adjust the composition of the Participants Committee to reflect a higher proportion of Private Sector Participants in the Prototype Carbon Fund than was originally envisaged; and (2) clarify that the PCF operations are subject to the Operational Policies of the World Bank Group. A draft Resolution detailing these amendments, for approval by Executive Directors, is contained in Attachment 1.

3. Also for information, the FY01 Business Plan and Budget of the Prototype Carbon Fund is contained in Attachment 3.

**B. PCF Briefings to GEF Members and Parties to the UNFCCC**

4. On May 10, 2000, in consultation with Mr. El-Ashry, Chief Executive Officer of the GEF, PCF management provided the GEF Council members with a comprehensive report on the status of PCF implementation. In September 2000, the PCF Fund Management Unit organized a side event during the 13<sup>th</sup> meeting of the UNFCCC Subsidiary Bodies (SB-13). The PCF organized a similar side event in November at the Sixth Conference of the Parties to the UNFCCC (“COP-6”) in The Hague. At these events PCF staff presented the experiences gained thus far. Both side events were well attended and led to substantial follow-up discussion and increased use of the PCF web-site. PCF’s “lessons learned” have also been documented and made public through the PCF web-site at [www.PrototypeCarbonFund.org](http://www.PrototypeCarbonFund.org).

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<sup>1</sup> PCF’s “*First Report Prototype Carbon Fund Implementation and Proposed Amendment to the Instrument Establishing the Prototype Carbon Fund*” (May 4, 2000) is numbered R2000-69.

## **C. Progress with PCF Implementation**

### **C.1 Second Closing and Final Status of Fund Subscription**

5. **The Second Closing** of the Fund occurred on October 31, 1999. Two additional private sector Participants joined the Fund - Fortum from Finland and Rabobank from the Netherlands, bringing the number of Fund subscribers to six public sector Participants and seventeen companies. Final subscription to the PCF is *US\$ 145 million*, US\$ 35 million below the maximum Fund size. As per the PCF Instrument, the IBRD as PCF Trustee may, at any time and with the approval of Participants, solicit voluntary supplementary contributions from Participants provided however, that the aggregate amount of contributions to be made to the Fund (including the voluntary ones) does not exceed the revised US\$ 180 million maximum size, approved by the Executive Directors in May 2000.

### **C.2 Meetings of Participants and Host Countries**

6. Since May 2000, the PCF has held: four Participants Committee meetings (June 2000, September 2000, November 2000, and February 2001); one Annual Meeting of the Participants (June 2000); one Technical Advisory Group meeting (September 2000); and two Host Country Committee meetings (June 2000 and February 2001). At the Annual Participants meeting in June, the FY01 Budget was approved (see Attachment 3), along with a contingency financing plan. Pursuant to the PCF Instrument, Participants also agreed to make a performance-linked payment to the IBRD, reflecting what they called "the excellent performance of the Prototype Carbon Fund (...) since its commencement of operations". The PCF's governance structure appears to operate effectively and efficiently in serving PCF's mandate. During this intensive series of meetings, it was apparent that joint meetings of the public and private sector Participants with Host Country representatives on policy and project related matters have high value. The PCF's annual and periodic meetings have been restructured in order to facilitate more interaction between these groups.

### **C.3 Refinement of PCF Operational Modalities and Procedures**

7. **COP-6 Outcomes.** Prior to CoP-6 meeting in The Hague, in November 2000, PCF Participants and management expected that agreement on the guidelines, modalities and procedures for the flexible mechanisms of the Kyoto Protocol, would lead to a set of final adjustments to PCF policies and procedures, to ensure that PCF operations were in compliance with the requirements for Article 6 ("Joint Implementation" or "JI"; projects in countries with economies in transition) and Article 12 (the "Clean Development Mechanism" or "CDM"; projects in developing countries) of the Kyoto Protocol. However, the Parties to the UNFCCC were unable to reach an agreement in November 2000, and negotiations were suspended until Summer 2001, when COP-6 will resume. In the meantime, PCF Participants requested the PCF's Fund Management Unit to review the implications for the PCF of the current drafts of the Decision Texts. Discussions with Participants of the analysis by PCF staff of these implications took place in February, 2000, in Washington DC. It was agreed *inter alia* that in the interim, the risks and uncertainties for PCF financing had actually increased. Hence, while negotiations among

the Parties to the UNFCCC continue, PCF management will closely follow these negotiations, analyze plausible outcomes, and systematically alert Participants to the risk that greenhouse gas emissions reductions generated by PCF Projects may not meet the future requirements of JI and CDM, and, therefore, may not be able to be used by PCF Participants to meet their greenhouse gas emission reduction obligations under the Kyoto Protocol. For example the current negotiating text includes a number of options for the interpretation of "additionality" which would directly affect the establishment of baselines for PCF Clean Development Mechanism projects. Notes on these issues are available on the PCF website.

8. **PCF Implementation Notes.** The PCF's Fund Management Unit has prepared and refined a series of PCF Implementation Notes, building on the experience gained from the development and negotiation of the first PCF project (the Liepaja Solid Waste Management project in the Republic of Latvia) and from the preparation of a large number of other projects from which the PCF will possibly purchase greenhouse gas emission reductions. It is intended that these PCF Implementation Notes will guide PCF operations on matters such as pricing policy, portfolio development, and preparation and validation of baselines to achieve environmentally credible greenhouse gas emissions reductions<sup>2</sup>. In addition, the PCF Implementation Notes are part of the effort to share publicly the knowledge gained by the PCF; they can be found in the public domain of the PCF website at [www.PrototypeCarbonFund.org](http://www.PrototypeCarbonFund.org).

#### C.4 PCF Projects and Portfolio

9. **Project pipeline.** From only a few potential projects under serious consideration in May 2000, the PCF is now confronted with a large number of high-quality project proposals. The current pipeline extends to all regions of the world, covers a large variety of climate-friendly clean technologies in more than 30 projects, and comprises over US\$ 300 million in proposed greenhouse gas emissions reductions financing. In the Latin America and Caribbean region alone, proposals for PCF financing exceed US\$ 100 million in possible purchases of greenhouse gas emission reductions. The PCF is modest in scale – originally designed to undertake only 10-15 projects globally – and established with the objective, *inter alia*, to share with the Parties to the UNFCCC and other interested parties the knowledge gained in the course of Fund operations during the period when the guidelines, modalities and procedures that will govern JI and CDM are being negotiated. It has now become apparent that, for governments and key local stakeholders, undertaking the first greenhouse gas emissions reductions purchase transaction can be a very powerful capacity building experience.

10. In the face of excess demand for PCF financing, the Participants Committee reviewed and agreed to the PCF's revised portfolio strategy. Instead of achieving PCF portfolio's objectives for regional distribution by dollar volume of ER purchases, regional distribution objectives will now be achieved through numbers of projects. As a result, the portfolio will now contain a greater number of projects (about 25-35) which will be

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<sup>2</sup> During the reporting period the following PCF Implementation Notes were added: Implementation Note No.5 "Price Formation In PCF Emissions Reductions Purchases," and Implementation Note No.6 "Preliminary Validation Manual."

smaller in dollar size. The positive outcome of this shift is that it will allow PCF to further diversify its learning experience by country and by technology. Commitment was also made to support: purchases of greenhouse gas emission reductions from small-scale distributed photovoltaic power in such applications as rural households; and transport energy efficiency technologies to demonstrate how PCF financing can simultaneously support climate change mitigation and air quality improvements in cities. Finally, given that renewable energy projects dominate the current pipeline, Participants urged that adequate support be given to energy efficiency and fuel switching measures in the pipeline.

11. **Latvia's Liepaja Solid Waste Management** project was the first PCF project to reach the appraisal and negotiations stage. Technical discussions for both the IBRD's underlying project and the PCF component, took place during the week of April 10, 2000. The underlying project was approved by the Board on September 14, 2000. Both the Loan Agreement for the underlying project, between the Republic of Latvia and the IBRD, and a "Emissions Reduction Purchase Agreement" ("ERPA") for the PCF component, were signed on December 19, 2000. Because the Republic of Latvia is included in Annex I to the Kyoto Protocol, the project is considered to fall within the scope of Joint Implementation. The project allowed the PCF to pioneer the first baseline validation protocol. Experience in having the Liepaja Solid Waste Management project's baseline and "Monitoring and Verification Protocol" validated by an independent third party, allowed the PCF Fund Management Unit to prepare a preliminary validation manual. All documentation developed for the Latvia project is now published on the PCF's website. Website user statistics indicate that this information is in frequent use by the private sector and other stakeholders.

12. **Advanced Preparation.** In addition to the project in the Republic of Latvia, three projects have been approved for advanced preparation by the Fund Management Committee and cleared by the Participants Committee: Jamaica, Morocco, and Uganda. Six prospective projects in the pipeline are expected to be presented to the Participants Committee for review and clearance in June, 2001, including technologies such as fuel-switching, small scale crop-residue power and small run of river hydro. Fully-executed ERPAs are expected from as many as three of these operations by the end of Summer 2001.

## C.5 Communications and Outreach

13. **Consultations.** In adopting processes to achieve high quality greenhouse gas emissions reductions, the PCF Fund Management Unit has been working closely with UNFCCC Secretariat staff, consulting researchers and NGOs, and responding to requests for consultations from policy analysts and negotiators from among the Parties. In response to these requests, the PCF Fund Management Unit prepared and published in the PCF website in advance of COP-6 a note on lessons learned from PCF implementation. Among the most important findings so far is that the transaction costs of complying with the emerging guidelines, modalities and procedures for JI and CDM under the Kyoto Protocol put small scale power and energy efficiency measures, and hence small countries, at a large disadvantage. Many renewable energy technologies also appear to be adversely affected by the emerging guidelines. PCF's experience suggests that there

should be concern about the general complexity and number of transactions required to achieve environmentally credible greenhouse gas emissions reductions; this complexity might reduce the level of private investment that could otherwise be generated in developing countries in cleaner technologies with important local and climate benefits.

14. **The PCF*plus* Program** was launched to supplement the work of the PCF in the areas of outreach, research, and training. The program draws on interest income of trust funds from Canada, Finland and Sweden administered by the IBRD. A primary objective of PCF*plus* Program is to build capacity of Host Countries to realize opportunities in the evolving market for carbon. Outreach and training to Host Countries is achieved through PCF*plus* funding for pre- and post-negotiations workshops and other Host Country workshops where training is provided on aspects of CDM and JI design and implementation. In addition, from April 2001 onwards, the PCF*plus* Program will support a Kyoto Protocol training specialist in WBI to implement training activities during Host Country workshops and assist in the dissemination of practical lessons learned from PCF implementation.

15. **PCF*plus* Fellowships.** The PCF*plus*Program supports fellowships for Host Country representatives and for NGO members of the PCF's Technical Advisory Group from developing countries and countries with economies in transition. Fellows come to Washington, DC to work with the PCF's Fund Management Unit. A stipend and expenses are provided and Fellows agree to contribute to a review of aspects of the Kyoto Protocol relevant for their own country's implementation of the Kyoto Protocol or to PCF implementation, or to work on specific PCF operations. Because of the large amount of interest, this fellowship program is booked almost a year in advance already. A parallel PCF Participant fellowship program is also well underway; however, Participants provide their own funding for the duration of their stay with PCF.

#### **D. Proposed Amendments to the PCF Instrument**

16. This section outlines the context and justification for the proposed amendments to the Instrument establishing the PCF: (1) to adjust the composition of the Participants Committee to reflect a higher proportion of Private Sector Participants in the Prototype Carbon Fund than was originally envisaged; and (2) to clarify that the PCF operations are subject to the Operational Policies of the World Bank Group (please see the Draft Resolution in Attachment 1).

17. In compliance with the Instrument Establishing the Prototype Carbon Fund, the first of these proposed amendments has received prior unanimous consent from Participants at their meeting of June 2000 (see Resolution No. PM 2000-9 in Attachment 2); the second proposed amendment does not require such consent, as it is deemed not to adversely affect the rights of any Participant.

18. **Composition of the Participants Committee.** Under the terms of the current PCF Instrument, the size of the Participants Committee will have to be reduced from 7 to 5 members after its first term, expiring in June 2001. The Instrument also stipulates that the Participants Committee will be comprised of three private sector and two public sector representatives in its second term, with the ratio alternating each year thereafter. At their

first annual meeting, Participants indicated that they wished to retain the committee's size at the higher level of seven members due to the much larger-than-anticipated number of PCF Participants. Moreover, they felt that it should be left to them to decide which constituency should be in the majority in any term. Accordingly, they passed a resolution to this effect (Attachment 2) and requested the Bank's management to propose to the Executive Directors that these changes to the Instrument be made before the second annual meeting of the Participants.

19. **Bank Group Operational Policies.** At its design stage, it was envisaged that the PCF would largely have to support and build on projects from the World Bank's portfolio, and that only a few projects would originate from third party private and public sector project sponsors with neither IFC nor IBRD underlying projects. As it turns out, a significant proportion of the PCFs's portfolio can now be composed of the latter category. For IFC to supply environmental and social review service to the PCF would increase the level of quality assurance for these private sector PCF operations. However, requiring IFC sponsored PCF operations to comply with IBRD (as opposed to IFC) policies and procedures, makes IFC's participation in the PCF impracticable. Similarly, the IFC has agreed in principle to undertake environmental and social review for PCF third-party private sector projects. Again, making it possible for IFC to supply this environmental and social review service would increase the level of quality assurance for these private sector PCF operations.

**Recommendation:**

20. I recommend that, in the light of the foregoing, the Executive Directors adopt the Resolution provided in Attachment 1 to this memorandum, amending the Instrument Establishing the Prototype Carbon Fund.

James D. Wolfensohn  
President  
by Zhang Shengman

**INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT**

DRAFT RESOLUTION NO. [ \_\_\_\_\_ ]

**ON CHANGING THE COMPOSITION OF THE PARTICIPANTS COMMITTEE  
AND ON CERTAIN OTHER AMENDMENTS TO THE  
INSTRUMENT ESTABLISHING THE PROTOTYPE CARBON FUND**

**WEREAS** in accordance with Section 15.3 of the Instrument Establishing the Prototype Carbon Fund set forth in Resolution No. 99-1 and amended by Resolution No.2000-1 ("the Instrument"), the Instrument may be amended by the Executive Directors of the International Bank for Reconstruction and Development ("IBRD") with the prior unanimous consent of Participants;

**WHEREAS** Participants in the Prototype Carbon Fund by Resolution No. PM 2000-9 of their meeting of June 28, 2000, have given prior unanimous consent to amend the Instrument in accordance with the terms set forth in that resolution;

**WHEREAS** in accordance with Section 15.3 of the Instrument, the Instrument may also be amended by the IBRD as trustee of the Prototype Carbon Fund, without prior notice to or consent from any Participant, if such amendment is (i) to supply any omission, or cure, correct or supplement any manifest error or ambiguous, defective or inconsistent provision hereof, or (ii) for any other purpose which does not adversely affect the rights of any Participant; provided, that all Participants are notified of any such amendment within 15 days after the effective date of such amendment;

**NOW THEREFORE IT IS HEREBY RESOLVED AS FOLLOWS:**

The Executive Directors hereby amend the Instrument in the manner provided in Annex I to this Resolution.

**ANNEX I to Resolution [ \_\_\_\_\_ ]**

**Amendments to the Instrument Establishing the Prototype Carbon Fund**

**1. The following provision is deleted from Article I, Definitions:**

40) "Operational Policies and Procedures" means those policies and procedures included within the IBRD's Operational Manual from time to time;".

**2. Article I, Definitions: provisions 41-64, are renumbered as 40-63.**

**3. The following provision is included in Article I, Definitions:**

"64) "World Bank Group Operational Policies and Procedures" means the environmental and social operational policies and procedures of the institution of the World Bank Group which conducts the environmental and social review of the Project and which are in effect at the time of such review and the operational policies and procedures of the IBRD in other areas."

**4. Section 3.4 is replaced to read as follows:**

"Section 3.4. Compliance with ~~IBRD's~~World Bank Group Operational Policies and Procedures. The operations of the Fund shall comply with the World Bank Group Operational Policies and Procedures ~~of the IBRD~~, except to the extent that such operational policies and procedures may be inconsistent with the guidelines, modalities and procedures adopted by the Parties to the UNFCCC regarding the procurement of services by Independent Third Parties, in which case the latter shall govern."

**5. Paragraph b) of Section 5.1, Participants' Meetings, is replaced to read as follows:**

"b) reviewing and approving by two-thirds majority of the votes of the Fund any amendments to the Project Selection Criteria or the project Portfolio Criteria, other than amendments that in the Trustee's opinion are merely technical in nature; provided, that any such amendment shall be consistent with the World Bank Group Operational Policies and Procedures ~~of the IBRD~~ in the opinion of the Trustee and otherwise acceptable to the Trustee;".

**6. Paragraph (a) of Section 6.1, Participants' Committee, is replaced to read as follows:**

"(a) At the organizational Participants' meeting, the Participants will establish a Participants' Committee, which shall be comprised of seven members ~~during its first term and five members thereafter~~. The members of the Participants' Committee shall be officers, directors, employees or officials of Participants; provided, that not more than one member shall be a representative of the same Participant. The members of the Participants' Committee shall be elected by majority vote of the votes cast at a Participants' meeting. At the organizational Participants' meeting, the Participants shall elect members of the Participants' Committee for a term running from such meeting to the date of the second annual Participants' meeting. At the second annual Participants' meeting and at each annual Participants' meeting thereafter, the Participants shall elect members of the Participants' Committee to be members until the next succeeding annual Participants' meeting. The Participants' Committee shall elect one of its members to serve as chairperson until such time as such member has ceased to be a member of the Participants' Committee or until such member's successor as chairperson has been elected."

**7. Paragraph (c) of Section 6.1, Participants' Committee, is replaced to read as follows:**

"(c) The Participants' Committee elected at the organizational Participants' meeting shall be comprised of four members who are officials of Public Sector Participants and three members who are officers, directors or employees of Private Sector Participants. The Participants' Committee elected at the second annual Participants' meeting shall be comprised of ~~two~~three members who are officials of Public Sector Participants and ~~three~~four members who are officers, directors or employees of Private Sector Participants. Thereafter, the representation of Public Sector Participants and Private Sector Participants on subsequent Participants' Committees will alternate annually between ~~two~~three and ~~three~~four members, respectively, unless the Participants shall decide unanimously to adopt an alternative procedure."

**8. Section 8.8, Fund Management Unit, is replaced to read as follows:**

"Section 8.8. Fund Management Unit. A Fund Management Unit shall be established by the Trustee. The Fund Manager shall head the Fund Management Unit as the chief executive officer and shall have overall responsibility for the day-to-day operations of the Fund, including, without limitation: (i) overseeing the operations of the Fund Management Unit, including the selection of its staff; (ii) representing the Fund's interests at international fora and maintaining contact with Participants and Recipients; (iii) overseeing the selection of Projects, reviewing Projects during their appraisal,

implementation and operation, and negotiating Project Agreements; (iv) ensuring compliance with Project Selection Criteria and Project Portfolio Criteria; (v) seeking to ensure consistency, to the extent possible, of the Fund's operations with the regulatory framework of the UNFCCC and the World Bank Group Operational Policies and Procedures; and (vi) collecting, organizing, managing and disseminating the knowledge and information obtained by the Trustee in the course of its operation of the Fund."

9. For ease of reference only, the deleted text has been included above and the changes made to the original text have been underlined.

**PROTOTYPE CARBON FUND**

**PARTICIPANTS' MEETING**

**June 28, 2000**

**Resolution No. PM 2000-9**

**Increase in Size of the Participants' Committee**

Whereas, the Participants consider it desirable that the composition of the Participants' Committee be adjusted to reflect a higher proportion of Private Sector Participants in the Prototype Carbon Fund than originally envisaged;

**RESOLVED:**

1. THAT starting with the second annual Participants' meeting, the size of the Participants Committee shall be set at seven members rather than five, as currently specified in the Instrument Establishing the Prototype Carbon Fund (the Instrument), by adding one member who is an official of a Public Sector Participant and one member who is an officer, director or employee of a Private Sector Participant;
2. THAT for the election to be held at the second annual Participants' meeting, the Participants' Committee shall be comprised of four members who are officers, directors or employees of Private Sector Participants and three members who are officials of Public Sector Participants;
3. THAT the Trustee is hereby authorized to submit an amendment to the Instrument, reflecting the decisions described in (1) and (2) above, for the approval of the Executive Directors of the International Bank for Reconstruction and Development and, if approved, to revise the Instrument accordingly;
4. THAT a decision on whether to continue to alternate annually between majority representation by Public Sector Participants and Private Sector Participants on the Participants' Committee following the second annual Participants' meeting, as currently provided for in the Instrument, shall be taken by the Participants prior to or at such meeting.

**PROTOTYPE CARBON FUND**

**BUSINESS PLAN AND BUDGET**  
**JULY 1, 2000 - JUNE 30, 2001**  
**(FY01)**

For Review At the Annual PCF Participants Meeting,  
June 27-28, 2000  
Paris, France



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The Prototype Carbon Fund (PCF) is a private-public partnership that aims to mobilize new and additional resources to address climate change and promote sustainable development. The PCF is capitalized in a first closing at US\$135 million as of April 10, 2000, with six governments and fifteen companies participating<sup>1</sup>. While project identification and preparation activities have been well underway for the past two years, PCF operations formally started on April 3, 2000. At the Organizational Meeting of the PCF on April 11 and 12, Participants resolved that, subject to Bank Board approval, the Fund should offer a second closing to named companies by mid-July, 2000. On May 15<sup>th</sup>, the Bank's Board approved this change in the PCF's Instrument and the second closing candidate companies were duly informed.<sup>2</sup>

A report on the status and anticipated outcomes of second closing will be made to the First Annual meeting of Participants in Paris on June 27 -28, 2000.

## I. FUND OBJECTIVES AND STRATEGY

### A. Business Objectives

The PCF has three primary strategic objectives (adapted from the Information Memorandum, p. 11):

1. Show how project-based emissions reduction (ER) transactions and trade can promote and contribute to sustainable development and lower the cost of compliance with the Kyoto Protocol;
2. Provide the Parties to the UNFCCC, the private sector, and other interested parties with an opportunity to "learn by doing" in the development of policies, rules and business processes for the achievement of emissions reductions under CDM<sup>3</sup> and JI;
3. Demonstrate the potential for public-private partnership in mobilizing new resources for addressing global environmental problems through market-based mechanisms.

In fulfilling these objectives the PCF seeks to create shareholder value through two products:

- high quality emissions reductions at or below a price of \$20/ton/Carbon, or \$5/t/CO<sub>2</sub>;
- knowledge and information about business processes, good practice, and policy that help both the private and public sector efforts for developing a market in emissions reductions under the Joint Implementation (JI)/Clean Development Mechanism (CDM) framework.

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<sup>1</sup> Participating governments are Canada, Finland, the Netherlands, Norway, Sweden, and the Japan Bank for International Cooperation (JBIC). Companies include BP Amoco, Chubu Electric Power Company, Chugoku Electric Power Company, Deutsche Bank, Electrabel, Gaz de France, Kyushu Electric Power Company, Mitsubishi Corporation, Mitsui & Co., Norsk Hydro, RWE, Shikoku Electric Power Company, Statoil, Tohoku Electric Power Company, and Tokyo Electric Power Company.

<sup>2</sup> Companies registering for a second closing include Fortum, Shell Canada, DaimlerChrysler, Nippon Mitsubishi Oil, Sumitomo Corporation, HydroQuebec, EBX, Espoon Sahko Oy and partners, and RaboBank.

<sup>3</sup> Article 12 of the Kyoto Protocol describes the purpose of the CDM as "... to assist Parties not included in Annex I in achieving sustainable development and in contributing to the ultimate objective of the Convention, and to assist Parties included in Annex I in achieving compliance with their quantified emission limitation and reduction commitments under Article 3".

<sup>4</sup> More precisely, PCF is seeking to achieve a price outcome of \$20/t/Carbon or about \$5/t/CO<sub>2</sub> across the portfolio. (The exact price outcomes will not be known until Fund termination in 2012). To achieve this price outcome, PCF management is seeking deals with a cost of production of carbon up to \$10/t/carbon or about \$3/t/CO<sub>2</sub>.

If these objectives and products are achieved, the PCF should also demonstrate, inter alia, that:

- the economies of Bank client countries can benefit from capturing substantial resource rents from trade in greenhouse gas emissions reductions;
- the profitability of cleaner and more efficient technologies in energy, industry and transport will increase, stimulating transfer of these technologies to the energy, industrial and transport sectors in Bank client countries; and that
- there are important local and regional environmental, health and welfare benefits associated with investments that achieve greenhouse gas emissions reductions.

## II. PORTFOLIO DEVELOPMENT

The Information Memorandum of the PCF provides general guidance on project selection such as achieving a broad balance in the number of projects undertaken in economies in transition and in developing countries (JI and CDM). The PCF is to place emphasis on development of renewable energy and energy efficiency projects, which will promote sustainable development. The portfolio development strategy for PCF investments was discussed with Participants at the First Organizational Meeting. The finalized PCF Implementation Note on Project Portfolio Development Strategy now reflects the Participants' preferences and guidance on an operational interpretation of the project selection criteria agreed for the Fund. The PCF Fund Management Unit (FMU) will aim to achieve a 3:2 ratio between renewable energy and energy efficiency in the PCF portfolio based on the guidance provided by the Participants. The resource allocation guidance provided would result in about 20 PCF projects being prepared and approved by mid-2003.

An initial set of projects is being identified and prepared by the World Bank. In addition, the International Finance Corporation (IFC) has started due diligence on projects proposed by the private sector. A number of third party projects, including those proposed by the Participants in the PCF, are anticipated in the PCF's portfolio. A list of the projects and the status of preparation is provided to the Participants on the website and updated monthly by the FMU.

It is anticipated that as much as 75% of PCF projects must be identified and cleared for further development by the end of calendar year 2001 (CY01) if PCF funds are to be placed in approved investments by mid-2003. The dynamic nature of the business and the differing speed with which project development proceeds indicates that changes in the status of the pipeline are likely. The FMU intends to actively inform and seek advice from the Participants Committee on a regular basis on the project portfolio development.

The current pipeline of the PCF consists of host country endorsed projects in:

1. Latvia (Liepaja Region Solid Waste Management);
2. Costa Rica (Fund for Renewable Energy Resources), and;
3. Uganda (Renewable Energy Small-scale Power Generation for Decentralized Rural Electrification).

Early project identification is in progress in Poland, Slovak Republic, Czech Republic, Brazil, Mexico, Colombia, India, Morocco, Egypt and other countries.

**Monitorable progress indicators** for the period July 2000 through June, 2001 are as follows:

- The level of effort in project identification will increase substantially in line with the preferred portfolio development strategy and as summarized in Table 1 below;
- All approval processes for the Latvia Liepaja Region Solid Waste Management Project will be completed;<sup>5</sup>
- Participants Committee clearance of the Costa Rica FRER project will be sought at the June 2000 meeting, and all other approvals and preparation for the project will be completed in FY01;
- Uganda project will be appraised by the end of calendar year 2000 (CY00). All project preparations will be completed by March 2001.
- In addition to the three projects listed above, the FMU expects to reach appraisal stage for four additional projects. The projects taken to appraisal will depend on the results of the analysis of the baseline, appropriateness of PCF financing and other eligibility screening and endorsement by the host country government. The projects under consideration include:
  1. Poland or another Eastern European country: Energy efficiency project through established intermediaries (World Bank proposal);
  2. Czech Republic: Geothermal energy for district heating (World Bank proposal);
  3. India: Upgrade of distribution efficiency (IFC Proposal);
  4. Morocco: Wind power to replace oil and natural gas (World Bank or IFC proposal);<sup>6</sup>
  5. Egypt: Wind Power to replace natural gas (Third Party proposal);
  6. South Africa: Refuse-derived fuel to replace coal (IFC proposal);
  7. Colombia: Wind power to displace oil and coal (Third party proposal);
  8. Guyana: Bagasse-based cogeneration (IFC proposal);
  9. Argentina: Wind energy (IFC proposal);
  10. Mexico: Candidates include solar thermal for heating applications and cogeneration;
  11. Brazil: Candidates include biomass fuel for industrial process applications, cogeneration and renewable energy.

The evolving nature of the business and the differing speed with which project development proceeds implies that there will be changes in the anticipated order in which projects develop;

- The FMU intends to complete the review of 24 Project Idea Notes (PINs) in FY01 (see Table 1 below). Of these, 12 will be prepared into Project Concept Notes (PCNs), and presented to the Participants Committee. As indicated above, 7 of these 12 will reach the Project Appraisal Document (PAD) stage before the end of FY01.

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<sup>5</sup> Initial negotiations on the project, including the carbon purchase agreement, were held 10-14 April, 2000. Further discussions on the Carbon Purchase Agreement were held in May and June 2000. The Bank-financed component of the project was to be presented to the Board of the World Bank on June 1, 2001 but the current schedule expects this to happen on July 16, 2000.

<sup>6</sup> Both, the World Bank and IFC have been approached for support for wind energy investment in Morocco.

**Table 1: Regional Distribution of Project Pipeline Development Process and Budgetary Implications.**

Region	Total Processed in FY 2001		
	PIN <sup>7</sup>	PCN <sup>8</sup>	PAD <sup>9</sup>
Europe and Central Asia	6	4	2
Latin America	4	3	2
Africa	6	3	2
East Asia	4	1	
South Asia	4	1	1
<b>Total</b>	<b>24</b>	<b>12</b>	<b>7</b>
Estimated resources <sup>10</sup> required in FY 2001 ('000\$)	600	600	420

FY= Fiscal year, running from July 1 to June 30 .

- As shown in the Table 2 below, 5 of the 12 PCNs will still need further preparation at the end of FY01. PCNs will include the projects included in the PCF project pipeline document posted and updated monthly in the Participants' Discussion Area on the website. At the end of FY01, the pipeline will consist of 12 PINs, 5PCNs and 7 PADs.

**Table 2: Status of Project Pipeline Development**

<sup>7</sup> Project Idea Note: this column indicates the number of the number of PINs reviewed and posted on the Participants discussion area on the website.

<sup>8</sup> Project Concept Note: This column indicates the number of project presented to the Participants Committee, with Host Country endorsement letter, for approval. Approved PCN will become an annex to the standard World Bank Project Concept Document to be used for World Bank Management review.

<sup>9</sup> Project Appraisal Document: this column indicates the number of projects which will have the PAD ready for World Bank management review.

<sup>10</sup> The estimation of resources is based on average expenditure of \$25,000 for taking a PIN to a PCN, a further \$50,000 for taking a PCN to the PCF annex to the PAD and an average of \$60,000 more being required to complete preparation of the PCF component of a project for negotiations.

Region	Status of the pipeline at the end of FY 2001			Cumulative at or beyond PAD stage by end of FY 2001
	PIN	PCN	PAD	
Europe and Central Asia	3	2	2 <sup>#</sup>	3 <sup>@</sup>
Latin America	2	1	2 <sup>+</sup>	2
Africa	3	1	2 <sup>*</sup>	2
East Asia	2	1		
South Asia	2		1	1
<b>Total</b>	<b>12</b>	<b>5</b>	<b>7</b>	<b>8</b>

FY: Fiscal year, July 1 to June 30

- Completing the investment phase of the PCF by mid-2003 will require the FMU to identify three-fourth of the PCF portfolio by the end of 2001. The performance indicators presented in this business plan have been prepared with the objective of achieving this target. While all efforts will be made by the FMU to achieve these aggressive goals, it must be recognized that there may be factors beyond the control of the FMU which may not allow the goals to be achieved. The evolving and dynamic nature of the business creates risks of delays which are unique. These include completing procedures related to baselines, monitoring and verification protocol, validation and agreeing upon carbon purchase and transfer agreements.

### III. BUSINESS PROCESSES FOR PCF IMPLEMENTATION

#### A. Achieving ER Quality and Price Objectives

##### i. Emission Reductions: CERs and ERUs

The primary product of the PCF is emission reduction units (ERUs) from JI projects between Annex I Parties under Art. 6 of the Kyoto Protocol (KP) and certified emission reductions (CERs) from CDM projects in non-Annex I countries under Art. 12 KP. In PCF business terminology, these are collectively referred to as Emissions Reductions (ERs). PCF ERs are to be high quality and reasonably priced, bearing in mind the Participants' expressed willingness-to-pay and the availability of cost-effective low risk projects to achieve emissions reductions.

Until further guidance from Parties and Participants, the PCF does not intend to differentiate its procedures between CDM and JI projects. Instead, based on current knowledge and remaining uncertainty of the emerging modalities for Art. 6 and 12 KP, the PCF has developed a common approach to project development and validation, monitoring and verification that is expected to meet future KP modalities and produce emissions reductions of high quality. PCF

<sup>#</sup> These will be from the projects in Poland or Czech Republic or Slovak Republic.

<sup>@</sup> Including the Latvia project in addition to three PADs remaining to be processed.

<sup>+</sup> In addition to Costa Rica, this would include one project from either Mexico or Colombia or Guyana.

<sup>\*</sup> Includes Uganda and one of the projects from South Africa, Egypt or Morocco.

Implementation Notes on establishing a process of verification and certification as the basis for further learning; project development and quality

## **ii. Meeting the Quality Objectives**

High quality ERs are defined as those that at the time a project is selected will be able to apply their shares to UNFCCC, related international

To ensure this dimension of ERs

- first, a definition of quality for JI and CDM projects in
- second, the establishment of and resulting ERs meet those

While awaiting further guidance from governments and others to

Implementation Notes on establishing baselines and environmental additionality, and on the process of verification and certification, are available on the PCF website. These documents are the basis for further learning; updates will be provided as experience grows and the PCF's project development and quality assurance system develops.

## ii. Meeting the Quality Objective for PCF ERs

High quality ERs are defined as being of a sufficient quality so that in the opinion of the Trustee at the time a project is selected and designed, there will be a strong likelihood that Participants will be able to apply their share of ERs for the purpose of satisfying the requirements of the UNFCCC, related international agreements or applicable national legislation.

To ensure this dimension of ER quality requires:

- first, a definition of quality criteria and indicators that appropriately reflect the requirements for JI and CDM projects in Art. 6 and 12 KP respectively and,
- second, the establishment of a formalized process to objectively assess whether the project and resulting ERs meet those criteria and requirements.

While awaiting further guidance from the Parties, the PCF is collaborating with host governments and others to explore and apply satisfactory criteria for additionality and sustainability for each PCF project, and indicators to conservatively estimate baseline emissions and ERs, and report on sustainable development outcomes.

Concerning process, some comfort can be taken from the consistency between the approach emerging from the UNFCCC discussions about Art. 6 and 12 KP modalities and the PCF's own approach. In summary, the key measures under consideration for Article 12 transactions include:

1. Development and explanation of the project baseline in a baseline study to be undertaken as part of the feasibility study for the project.
2. Development of a Monitoring and Verification Protocol (MVP) for each project that specifies observable indicators and defines the method to determine achieved emission reductions.
3. Validation of the project's design, in particular baseline and MVP by an independent third party.
4. Periodic verification of emission reductions by a different independent third party through a professional audit and verification process.

The PCF's project agreement ensures that the project entity monitors the specified indicators and calculates emission reductions as defined by the project MVP. The agreement also ensures that the PCF, and any independent third party selected for this purpose, has access to the project documentation, and all relevant information. The FMU receives detailed validation and verification reports and a formal statement (certificate) by the validation/verifier about their findings. The FMU will report this information to the UNFCCC and register the project in accordance with UNFCCC requirements.<sup>11</sup>

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<sup>11</sup> Presently, there is no differentiation between Art 6 and Article 12 transactions for the PCF. While the modalities for the generation of ERUs and CERs have not yet been defined and decided on by the Parties to the Kyoto Protocol, it is apparent that they will differ markedly for the two mechanisms. ERUs are expected to feature less stringent requirements as regards the baseline for the JI project and the verification of emission reductions from that project, because the transfer of ERUs by a project host country will lead to an equivalent reduction in the transferring Party's budget of assigned GHG amounts (AAUs). Whether ERUs will be equivalent with AAUs has not yet been determined. However, no objections are

It is expected that the process outlined above will be sufficient to meet future Art. 6 and 12 KP standard. The FMU will maintain close contact with the Parties and the UNFCCC Secretariat, the CDM Executive Board and other designated entities, to ensure that every necessary adjustment will be made to bring all ERs obtained and held by the PCF in line with new guidance and UNFCCC requirements. As the negotiations progress, the FMU will report to Participants on the decisions the Parties make or fail to make, on the impact of these decisions on the quality of projects in progress and expected ERs, and on any modifications the FMU will make to the quality assurance system to bring it in line with UNFCCC developments.

As discussed with Participants at the Organizational Meeting, the FMU has explored the opportunity to enhance the quality of PCF ERs using risk assurance instruments to cover a variety of political and technical risks. A presentation on this subject and possible next steps will be made to Participants at the June meeting.

**Monitorable progress indicators** for the period July 2000 through June 2001 are as follows:

- Issue a PCF Implementation Note on the PCF's approach to obtaining early credit for emissions reductions achieved prior to the commitment period in JI countries and report to Participants in due course on whether this Note should be adjusted in light of the outcomes of the Sixth Conference of the Parties to the UNFCCC (COP-6);
- Draw the lessons learned from validation of the Liepaja project and integrate them in improved business processes. In particular, complete work on a validation protocol, which includes a detailed list of specific project requirements that would have to be used in the validation process;
- Prepare and maintain a short list of qualified companies for validation, verification and certification services for the PCF;
- After Board approval of the Project, publish the Latvia Liepaja project baseline study, MVP and the validation opinion from Det Norsk Veritas;
- Actively participate in the UNFCCC workshops, SB-13, COP-6, and other informal consultations organized by the UNFCCC Secretariat and the Parties to ensure that every necessary adjustment will be made to bring all ERs obtained and held by the PCF in line with emerging guidance and UNFCCC requirements;
- Prepare a note for Participants on the outcomes of COP-6 concerning implications for the PCF's procedures and project selection criteria, and seeking Participants' guidance on the FMU's interpretations of needs for any specific changes that would appear to be required in PCF's operating modalities;
- Based on guidance from Participants on COP-6 outcomes, revise and reissue any affected PCF Implementation Notes as required for Participant, Host Country and other stakeholder review;
- On an ongoing basis, integrate lessons learned from PCF operations, and research results from *PCFplus*, into the PCF's operational procedures and project guidelines in consultation with Participants;

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expected to obtaining AAUs from the first commitment period budget of a host country for emission reductions achieved by a JI project before the first commitment period. The PCF will negotiate the transfer of AAUs for pre-commitment period reductions in its JI projects. A PCF Implementation Note on the PCF's approach to obtaining credit for ERs in JI countries certified before 2008 has been prepared in draft for review by Participants in their First Annual Meeting.

- Record agreed changes in PCF procedures and project selection criteria in semi-annual Participants reports; and,
- Commission and review with Participants specific risk assurance measures to enhance the value of PCF ERs.

### iii. Meeting the Price Objective for ERs

The price objective pursued by the PCF has a quantitative and qualitative dimension. The quantitative dimension pertains to the average dollar amount (price per ton of CO<sub>2</sub>) eventually<sup>12</sup> paid by the PCF for each valid ER from a particular PCF project. The qualitative dimension pertains to the equitable sharing of benefits from PCF projects between hosts and PCF participants and is defined by the satisfaction of both sides with the final outcome of the project, of which price is an important factor.

Following guidance from the Participants, the PCF attempts to negotiate a set of purchase agreements which, in aggregate, at the end of the Fund's life will result in an effective price for ERs obtained for Participants across the portfolio of about \$20 per ton of Carbon (or about \$5 per ton of CO<sub>2</sub>) in year 2000 prices. This portfolio average price outcome is regarded as the PCF's price objective and every attempt will be made to identify and develop projects and approaches to PCF investment, including competitive bidding for PCF ER financing, which could achieve this or a lower price of ERs to the Fund. In order to ensure this outcome and have flexibility to provide adequate incentives for project sponsors and governments selling emissions reductions to the PCF, and to hedge against risks inherent in specific projects, the PCF will strive to identify projects for further development with estimated costs of production of emissions reductions not exceeding \$10 per ton of Carbon.

The PCF attempts to ensure a fair and equitable, hence durable outcome of price negotiations by assisting the client in building capacity for negotiations. In order to prepare the Host country counterparts and project sponsors for price negotiations, consultations will take place as early as practicable on the international legal and market context of PCF financing of ERs. At the discretion of the host country, this process may include a pre-negotiations workshop, in which both PCF and host country representatives participate and present their analysis. In addition, the host country has access during and after the workshop to independent experts of its choice, who provide appropriate assistance to the host country negotiation team.

Finally, to enhance the transparency and quality of the process of ER price negotiations over time, and to maximize the learning value for diverse stakeholders from PCF implementation, Host Countries and project sponsors will be encouraged to co-sponsor with the PCF a post-negotiations workshop<sup>13</sup> wherever feasible. Such workshops will enable Participants and Host Countries to review the resulting agreements, business processes, and the associated issues and remedies. Post-negotiations workshops should also capture advice and experience from Participants and host governments, and provide valuable experience for later PCF projects and non-PCF projects.

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<sup>12</sup> The actual price paid for PCF emissions reductions in any one project will be known only at the end of the period of the project in which the PCF has an interest.

<sup>13</sup> Subject to the availability of grant assistance from donor governments through the PCF Holding Trusts and other sources to cover the costs of organizing and ensuring adequate participation of local and potentially regional stakeholders in this process.

**Monitorable progress indicators** for the period July 2000 through June, 2001 are as follows:

- Prepare a note on the anticipated price outcomes of buying ERs from each category and specific technology for alternative energy sources, supply- and demand-side efficiency measures, and fuel switching (i) up to 2012 and (ii) through 20 years of a PCF-project's life;
- Subject to government and project sponsor approval, make arrangements for a small number of Participants to observe on a first come first serve basis negotiations for projects reaching this stage during FY01;
- Finalize arrangements and invite Participants, Host Country Committee members and selected others to the Latvia post-negotiations workshop planned in Riga following the Bank Board review of the underlying IBRD project in July 2000<sup>14</sup>;
- Utilize expertise assembled at pre-negotiations workshops to conduct capacity building activities for other local and regional stakeholders. These activities would focus on the emerging market for ERs in the framework of the Kyoto Protocol, using the PCF's planned investment and implementation experience as a source of training materials. Pending acceptance of prospective donors for this program, the FMU will publish a work program for these capacity building activities, including arrangements to collaborate with others who would take primary responsibility for their design and delivery.

## **B. Implementation Process**

The Information Memorandum (pp. 27-28) describes the process of project selection and development, or the "project cycle". At the start of the PCF implementation phase in April, the project cycle was reviewed and updated to reflect the lessons learned from early project activities in Latvia and Costa Rica. A table was formulated, describing each step in the cycle, assigning responsibilities for tasks, indicating typical lead times for each step, and identifying the associated documents to be produced in each step, with examples of good practice. This project cycle process table is an element of the Operations Handbook.

In addition, a template was developed for the Project Idea Note (PIN), which includes minimum eligibility criteria. This template is available on the website and is now used by project proponents when submitting proposals for PCF funding.

The PIN Template is also an element of the PCF Operations Handbook, which is now routinely provided to project task teams and will be updated as more experience in PCF implementation develops. The Handbook is also used at Project Organizational Workshops conducted with project task teams after a PCF project idea is approved by the FMU, early notification given to the host government, and the GEF has decided not to exercise its right to take up the project. The Workshop is designed to brief the project task team on the PCF project cycle, specific PCF process requirements and safeguard policies, as well as to discuss the baseline concept in the context of the project concerned.

**Monitorable progress indicators** for the period July 2000 through June 2001 are as follows:

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<sup>14</sup> See footnote 12.

- Develop a set of formal training modules, specifically designed for potential host countries and project sponsors to help prepare them for the unique Kyoto Protocol-related steps in the PCF process and for the contract negotiations;
- Prepare a PCF Implementation Note on the process of ensuring compliance with Bank Group safeguards policies on environmental and social impact assessment in PCF projects from third party project suppliers.

## IV. MAXIMIZING THE VALUE OF THE KNOWLEDGE ASSET

### A. The PCF's Website

A key role of the PCF is to capture and disseminate the knowledge, information and lessons learned gathered from its experience to a wide group of stakeholders globally. At the same time, the PCF has an obligation to provide high value to its shareholders from the development of the knowledge asset in which they have invested.

PCF's website at [www.prototypecarbonfund.org](http://www.prototypecarbonfund.org) is expected to develop into the primary information and knowledge delivery vehicle for stakeholders globally, regardless of bandwidth and connectivity levels. In order to improve public access, the website is maintained on a server outside that of the World Bank. Activity on the site has averaged over 1,000 hits per day since it was established in October 1999, with peaks in activity occurring during the public launch in January and the first PCF Organizational Meetings in April.

To provide the capacity to meet the knowledge and information needs of Participants, Host Country Committee representatives, and TAG members, the PCF Team recently hired a full-time Knowledge Manager. This team member will manage the website, as well as communications and dissemination. In addition, posting and notification of documentation have been systematized. Important organizational, project, and informational documents are posted in public or private discussion groups, as appropriate, and PCF constituents receive an email notifying them of the posting. Currently, thirty-five Participants, two TAG members, and five Host Country representatives have registered at the website and are participating in private discussion groups.

The website also functions as the main vehicle for informing the public about the PCF and receiving feedback. The website has a Public Discussion Area, where public documents are posted. This discussion area provides a feedback ("Reply") function to allow anyone to comment on PCF activities. The template for the PIN is publicly available in the "Projects" section of the website, so that any third party may obtain and submit a project idea following the standard template. Third-party sponsors have been submitting project ideas to the website at a rate of one per week since early May.

The primary challenge for the next twelve months is to make this vehicle for communication and dissemination widely known and fully effective. In the first instance, this means reaching the primary target audiences, especially stakeholders in developing countries.

**Monitorable progress indicators** for the period July 2000 through June, 2001 are as follows:

- Develop a standard website marketing plan, which may include titling and keywording the website; registering with search engines; identifying and requesting reciprocal links, for example, to the UNFCCC website; and utilizing web mailing lists and news groups;
- Develop a portal page for all interested PCF participants for their own kiosks, which may include links to their website, activities in climate change, environmental management programs;
- Explore website features for auto-emailing documents and communications to registered users in developing countries; and,
- Consult internet experts on further ways to reach developing country audiences.

In the same period, additional activities will be undertaken to improve the website as an effective informational and interactive tool. These are:

- Create a section for private companies seeking to register to provide business services to the PCF, such as validation, risk assessment and advisory services for client consultations;
- Provide a site map to increase site usability;
- Expand the news section to include a "PCF in the News" section and a "This Week in PCF" section;
- Enable the database functions of the PCF website to allow for better organization and cross-referencing of all posted documents; and,
- Expand the Document Library to provide selected peer-reviewed, third-party documents about JI and CDM which the PCF Team deems important reference materials for policy makers and private sector analysts, e.g., carbon market assessments, synopses of CDM/JI design issues.

## B. Publications

The PCF Instrument Article X, Section 10.4 (p. 25) defines the formal reporting arrangements by the FMU to the Participants and the public. In addition to an Annual Report available to the public, twice-yearly status reports on PCF implementation (the Participants Reports) are to be made to PCF Participants. These reports will reflect on progress in implementation in accordance with the approved annual Business Plans and Budgets. Per the Information Memorandum (p. 47) Business Plans and Participants Reports are not available to the general public. The first Participants Report will be made available to Participants and Host Countries in advance of the First Annual Participants Meeting on June 27-28<sup>th</sup>, 2000.

**Monitorable progress indicators** for the period July 2000 through June, 2001, involving the release of PCF publications, are as follows:

- **Annual Report:** The Annual Report will be published in mid- to late October, following the availability of the audited statement of accounts in late September. As this is the only public report on progress with PCF implementation, it is effectively the PCF's flagship publication, and will have a high quality design and format similar to the existing formal documentation of the PCF, such as the Information Memorandum. It will also be available electronically on the PCF website. It will build on the content of the Participants Report to the First Annual Meeting and will be modified following Participants' review and updated to reflect progress through August 2000;
- **FY 01 Participants Reports:** The first FY01 Participants Report – the mid-year report - will be issued in early to mid-December 2000. The second FY01 Participants report will be

used to inform the Second Annual Meeting of Participants in June 2001, and will be issued with the draft FY02 Business Plan and Budget a month before the date of the Participants Meeting that year. All Participants Reports will be made available electronically and in a simply formatted printed form;

- **FY01 Business Plan:** Using the established format, the Second Annual Business Plan will be issued in May 2001, one month in advance of the date of the Second Annual Meeting of Participants;
- **PCF Implementation Notes:** The existing series of Implementation Notes<sup>15</sup> will be updated as needed following COP-6 in the Hague to reflect the agreements and guidance of the Parties on the rules and procedures for the implementation of Article 6 and Article 12 mechanisms, including rulings on eligibility criteria for projects qualifying under these;
- **PCF Lessons Notes:** Notes will be published on lessons learned in preparing, appraising and negotiating the Latvia PCF project, and the proposed Cost Rica and Uganda operations. These will capture for dissemination good practice and lessons learned in the focus, modus operandi, and sequencing of key PCF analytical, review and consultation steps towards negotiating carbon purchase agreements; and,
- **PCF Occasional Papers:** These will include background papers on the emerging policies, procedures, and market development, which provide the framework and market context for PCF business. They will include research outputs funded under PCF*plus* and papers arising from workshops and seminars conducted in support of PCF implementation.

The new Implementation Notes, Lessons Notes and Occasional Papers will be added to the Operations Handbook as they are finalized.

### C. Outreach, Consultation and Collaboration

In addition to internet-based knowledge and information sharing, the FMU intends to take opportunities that represent a cost-effective means for disseminating experience and discussing emerging good practice in market development for ERs. These will include opportunities designed specifically for Participants as co-financiers of the PCF as a means of exchanging views and maximizing synergies in learning between Participants and partners in Protocol-related activities.

**Monitorable progress indicators** for the period July 2000 through June, 2001 are as follows:

- PCF staff will present lessons learned and insights from PCF implementation, and exchange views with participants in UNFCCC scheduled workshops on policies and procedures at the SBSTA/SBI meetings in Lyon in September, at COP-6 in the Hague in November, and at any follow-up meetings of SBSTA/SBI through June 2001. PCF's contributions to these meetings will be posted for participants and archived subsequently for future reference;

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<sup>15</sup> The existing PCF Implementation Notes are on the following subjects: Portfolio Development Strategy, Working With Established Intermediaries to Support Small Economies and Small Projects, Baseline Methodologies for PCF Projects, and Validation, Verification and Certification for PCF Projects.

- PCF Participants will be invited to participate in PCF project missions and related activities. Those already identified include the Latvia Post-Negotiations workshop and a workshop in Costa Rica on the outcome of PCF negotiations and the plans for specific project financing;
- PCF staff and collaborating specialists will respond on a first-come-first-serve basis to requests by Participants to provide seminars and consultations on PCF-related business issues and lessons learned through PCF implementation. For example, RWE has scheduled a consultation on the energy-environment interface and the PCF on September 29<sup>th</sup>, 2000, in Duesseldorf;
- PCF staff will participate in conferences and workshops that offer important opportunities for raising awareness of PCF implementation, for pursuing prospective PCF deals with project sponsors and financiers, and for disseminating lessons learned and feedback on PCF practice;
- A second Technical Advisory Group (TAG) meeting will be convened around COP-6 or subsequent SBI/SBSTA meetings and asked to provide feedback on issues of portfolio development, baselines and additionality;
- Discussions on collaborative research and demonstration activities under PCF<sup>plus</sup> and other relevant World Bank climate change programs will continue with bilateral agencies in France, Canada, USA, and the Nordic countries and outcomes will be reported to Participants.

## V. PCF BUSINESS ADMINISTRATION

### A. Corporate Governance

#### i. Participants Meeting and Committee<sup>16</sup>

At the organizational meeting, Participants elected the seven member Participants Committee, and at its first formal meeting on April 13, 2000, the Participants Committee elected its Chairman and decided on the modalities for interaction between them and the Fund Management Unit<sup>17</sup>. The First Annual Meeting of Participants will be in Paris on June 27-28, and the Participants Committee will meet the day before.

Issues of Governance and related modalities expected to be raised by Participants at the First Annual Participants Meeting include:

- In light of the expanded size of the Fund and additional corporate members, should there be a change in the composition and size of the Participants Committee beyond the tenure of the current Committee members?
- If the above is agreed, is there a role for informal observers in this interim period in anticipation of changes after June 2001?
- Where and when should the Second Annual Participants Meeting be held?

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<sup>16</sup> The role of the Participants Meeting and the Participants Committee are defined in Articles V and VI, respectively, of the PCF Instrument.

<sup>17</sup> These outcomes are posted on the PCF web site as summaries of the Organizational Meeting and Participants Committee meeting.

## ii. Host Country Committee<sup>18</sup>

The Host Country Committee (HCC) also met on April 13 and selected three observers to attend the First Annual Participants Meeting, and an observer to attend the Participants Committee meeting, both events to be held in June 2000.<sup>19</sup>

Since the last HCC meeting, Burkina Faso and Uganda joined the HCC, and discussions are underway within the government of several additional countries, including Indonesia and Morocco. Current Chairman of the HCC, Mr. Eduardo Dopazo, will host a lunch during the early June SBI/SBSTA meetings in Bonn of current and prospective HCC members in order to consolidate a core membership of at least 15 members.

## iii. Fund Management Committee

The Fund Management Committee (FMC) met to review the FY01 Business Plan and Budget for presentation to the Participants Committee and Participants Meeting in June. The FMC will be increasingly focused on PCF project options as FY01 progresses. The Africa region representative on the PCF has changed and during the plan period, there is expected to be a rotation of some of the regional representatives as the emphasis in deal flow is likely to shift to the Asia and Pacific region.

## iv. Technical Advisory Group (TAG)<sup>20</sup>

The first full meeting of the TAG is scheduled to take place around the SBI/SBSTA meetings in Bonn in early June 2000, and Participants will be informed of the outcome of discussions at their Paris meeting.

During the current Business Plan period, another face-to-face meeting of the TAG will be convened, pending availability of funds from Holding Trust Funds investment income. Membership of the TAG will also be slightly expanded, and some members will change during the period in order to broaden feedback and maintain a set of skills and experience amongst advisors to match the particular needs of the PCF at any given period.<sup>21</sup>

## B. Human Resources

The Fund Management Unit is a small business unit comprising Bank regular staff and secondees under various arrangements serving the PCF either full or part-time. In fact, only two Bank regular professional staff will bill all their time to the PCF administrative budget. As of

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<sup>18</sup> Article 7 of the PCF Instrument defines the functions of the Host Country Committee (HCC).

<sup>19</sup> The three HCC members that were selected to attend the First Annual Participants Meeting are: Ms. Ieva Saleniece (Latvia), Mr. José Luis Samaniego (Mexico), and Mr. Ajavo Ayite-Lo Nohende (Togo). Mr. Eduardo Dopazo (Guatemala) was elected as HCC observer to the Participants Committee meeting. At the Paris meetings in June 2000, there will be new elections for HCC observers to server during the FY01 business period].

<sup>20</sup> Christiana Figueres, Center for Sustainable Development in the Americas (CSDA), Jake Werksman, Foundation for International Environmental Law and Development, Grace Akumu, Climate Action Network (CAN)-Africa, Saleem ul-Huq, CAN-South Asia, Ned Helme, Center for Clean Air Policy (CCAP), Zhou Fengqi, Energy Resources Institute, China, Jim Leslie, International Institute for Sustainable Development (IISD), Eduardo Sanheuzza, CAN-Latin America, Asger Garnak, CAN-Europe and Inforse, Denmark, Geir Sjoberg, UNDP (as of March, returned to Government of Norway), and Lee Solsbery, World Business Council for Sustainable Development (WBCSD).

May 2000, the core staff of the FMU had not changed since the Organizational Meeting.<sup>22</sup> However, recruitment for the Principal Financial Specialist is well advanced and the candidate should be in place before the end of June 2000.

The PCF also draws on about 20 other specialists as needed throughout the Bank's operations, research, legal, climate change, private sector, energy and infrastructure, and the IFC. In addition, the staff exchange program, internal development assignments, summer internships, and secondment arrangements are being used to supplement the capacity of the PCF at very low cost during the peak years of its operational phase. An update on staffing will be provided in Paris in June.

**Monitorable progress indicators** for the period July 2000 through June, 2001 are as follows:

- A French Environmental Economist will be seconded, and his/her work program will be developed;
- The Finnish Seconded, Mr. Jari Vayrynen, will take up his post in the core team on July 15<sup>th</sup>;
- A Bank Young Professional Program staff member, Benoit Bosquet, will spend 4 months with PCF from November 2000; and,
- PCF management will encourage and accommodate Participants' requests for short-term visiting fellow assignments to the FMU.

In addition, the FMU is expected to move into its permanent office space during the Fall. This new space will accommodate all members of the team in one location.

## VI. FINANCIAL RESOURCES

### A. Budget

The estimated budget proposed for review and approval for Participants for FY01 is attached to this Business Plan.

The proposed Administration Budget, at \$1.73 million, is 24% higher than the \$1.4 million budget originally envisioned in the Information Memorandum.<sup>23</sup> However, as discussed with the Participants at the Organizational Meetings in April, the \$1.4 million amount was estimated on the basis of a total fund size of \$100 million. The current size of the Fund, at \$135 million is 35% larger, and could be up to 80% larger if the new cap of \$180 million were to be reached. Administrative expenses of a significantly larger Fund than originally

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<sup>22</sup> FMU core staff include Ken Newcombe, Senior Fund Manager, Odil Tunali-Payton, Energy-Environment Specialist and Business Operations Officer (90%), Johannes Heister, Economist (80%), Chandra Shekhar Sinha, Engineer and Energy Specialist (70%); Ikko Nishimura, Engineer and Urban Planning Specialist (50%), Hanneke van Tilburg, Dutch Government Seconded and international lawyer, Christina Reinhard, Environment-Communications Specialist and Knowledge Manager, Maritza Bojorge, Team Assistant, and Matt Krainic, temporary staff assistant.

<sup>23</sup> The Accounting Protocol study was requested by the Participants during the June Participants Meeting. The estimated cost of this study is \$75,000 + expenses and has been added to the original figure for the Administrative Budget of \$1.65 Million which was presented at the Participants Meeting. This additional expense brings the total cost for Administrative Expenses to \$1.73 Million. This change has been reflected throughout the Business Plan and Budget.

envisioned are inevitably higher in order to strengthen the capacity of the FMU to address the growing business needs and to assure the quality of the ERs.

A breakdown of administration expenses by category is provided in Table 3 below:

**Table 3: Administration Expenses by Category**

Salaries and Benefits for FMU	36%
Contracted Services, including policy, technical and legal advice	34%
Marketing and Outreach to Participants, UNFCCC and other stakeholders	8%
Meetings of the Participants and Host s	3.5%
Audit, Reporting, Communications, Website Enhancement	3.5%
Overheads	15%

Project-related expenses are estimated based on the portfolio development plans laid out in Section II. However, as these may change during the Business Plan period, the estimates on project-related expenses will also have to be revised.

In addition to the sources anticipated to come in during FY01, there is also an estimated carry-over of \$6.85 million from FY00. The carry-over is particularly high because Deutsche Bank decided to pay its entire \$5 million contribution up-front in FY00. This brought the total of drawdowns in FY00 to \$8.38 million, which, at an average of roughly 5% annual interest, earned \$70,000 in investment income in two months. A more accurate figure of what was spent in FY00 will be available in late June and provided to the Participants at the Annual Meeting.

At the First Annual Meeting in June 2000, Participants will be asked to:

- Approve the proposed budget for FY01 as presented below;
- Consider a performance-linked payment to the Trustee based on the performance of the Fund during the previous FY; and,
- Provide guidance on planning for contingencies. A proposed contingency financing plan will be circulated separately prior to the Meeting.

**PROTOTYPE CARBON FUND  
ESTIMATED BUDGET: JULY 1-JUNE 30, 2001 (FY01)**

<b>EXPENSES</b>		<b>SOURCES</b>	
<i>Administration Expenses</i>		<i>Drawdowns from Participants</i>	
	<i>US\$</i>		
<b>Salaries and Benefits of Fund Management Unit</b>	<b>614,339</b>	<b>Drawdowns from Participants</b>	<b>6,040,000</b>
<b>Contracted Services</b>	<b>593,000</b>	6 Public Sector Participants (@\$470K each)	2,820,000
Operational Policy and Economics Expertise <sup>1</sup>	164,000	14 Private Sector Participants (@\$230K each) <sup>14</sup>	3,220,000
Project Technical Appraisal <sup>2</sup>	201,000		
IFC Portfolio Coordination	23,000 <sup>3</sup>		
Legal Services	100,000		
Fund Management Committee <sup>4</sup>	30,000		
Accounting Protocol Study <sup>5</sup>	75,000		
<b>Marketing for the Second Closing</b>	<b>10,000<sup>6</sup></b>		
<b>UNFCCC Events: Travel and Workshops</b>	<b>75,000<sup>7</sup></b>		
<b>Other Travel: Conferences and Outreach to Participants</b>	<b>56,000<sup>8</sup></b>		
<b>Annual Meetings of the Participants and Hosts<sup>9</sup></b>	<b>60,000</b>		
<b>Reporting, Communications, Website Enhancement<sup>10</sup></b>	<b>50,000</b>		
<b>Independent Financial Audit</b>	<b>10,000</b>		
<b>Overheads<sup>11</sup></b>	<b>260,000</b>		
Office Occupancy	137,940		
Information Technology Maintenance and Support	48,400		
Equipment and Supplies <sup>12</sup>	30,100		
Other Indirect Costs <sup>13</sup>	43,560		
<b><u>Total Administration Expenses</u></b>	<b><u>1,728,339</u></b>		
		<b>Investment Income</b>	
		<b>Investment Income on FY01 Drawdowns</b>	<b>302,000</b>
		at 5% average annual interest rate	302,000

<b>Project-Related Expenses</b>		
<b>Preparation</b>		<b>1,870,000</b>
24 Project Information Notes (@\$25K each)		600,000
12 Project Concept Notes (@\$50K each)		600,000
7 PCF Annexes to the Project Appraisal Documents (@\$60K each) <sup>15</sup>		420,000
Further Expenses for PCF-specific Processes, As Required <sup>16</sup>		250,000
<b>Disbursements</b>		<b>2,870,000</b>
Latvia Liepaja Solid Waste Management		620,000
Costa Rica FRER		250,000
Egypt Wind Power <sup>17</sup>		500,000
India Upgrade of Distribution Efficiency		1,000,000
Argentina Wind Power		500,000
Supervision and Verification <sup>18</sup>		172,200
<b>Total Project-Related Expenses</b>		<b><u>4,912,200</u></b>
<b>Reimbursements to IBRD</b>		
<b>Reimbursement of Fund Development Costs to IBRD</b>		<b>400,000</b>
<b>Institutional Fees<sup>19</sup></b>		
<b>Central Unit Fees for Trust Funds<sup>20</sup></b>		<b>112,500</b>
<b>TOTAL EXPENSES</b>		<b><u>7,153,039</u></b>
<b>TOTAL SOURCES <sup>21</sup></b>		<b><u>6,342,000</u></b>

1 J. Heister at 80% (\$100K)+DEC staff @ 12 sw (\$54K) + Secondees + Summer Intern @10K  
2 C.S. Sinha @70% (\$86.5K), I. Nishimura @50% (\$23K), B. Bosquet @23.5K+PSI/HC Technical staff @12 sw (\$48K) + External Consultants (\$20K)  
3 \$460/day for 10 sw (50 days)  
4 3 x Level I staff @ 2 sw each (@5000/sw)  
5 The Accounting Protocol study was requested by the Participants during the June Participants Meeting. The estimated cost of this study is \$75,000 + expenses and has been added to the original figure for the Administrative Budget of \$1.65 Million which was presented at the Participants Meeting. This additional expense brings the

total cost for Administrative Expenses to \$1.73 Million. This change has been reflected throughout the Business Plan and Budget.

- <sup>6</sup> 2 trips to Europe @5K ea.
- <sup>7</sup> For each of 9/00, 11/00 and 6/01 SBI/SBSTA/COP-6 events: 5 staff@300 /day, 10 days + \$5K per ticket + 5K for hosting dinners, etc.
- <sup>8</sup> 7 trips @300/day, total of 10 days, + \$5K for each trip.
- <sup>9</sup> Assuming they are held in Washington DC. Includes airfare and per diem for 4 Host Country Observers for 4 days. Also includes FMU travel to an additional, mid-year Participants Committee meeting.
- <sup>10</sup> Design and printing for Annual Report, participants Reports (2), Business Plan, and reprinting for Instrument, Brochure and posters @\$25 K
- <sup>11</sup> @500/sw for 44 sws and 11 staff, including secondees.
- <sup>12</sup> Standard allocation (5% of total Overheads) plus 6 laptops purchased @3000 ea.
- <sup>13</sup> Includes representation and hospitality, translation, direct communications, etc.
- <sup>14</sup> Deutsche Bank has paid all of its \$5m contribution upfront in May 2000.
- <sup>15</sup> Includes PCF due-diligence on the Baseline Study (15K), MVP (25K), and Validation process (20K).
- <sup>16</sup> Includes potential expenses for due diligence on Third-Party projects.
- <sup>17</sup> Assuming the Egypt, India and Argentina PCNs are approved by the Participants Committee.
- <sup>18</sup> For each of the above projects, 6% of disbursements (as provided in the Information Memorandum).
- <sup>19</sup> Including Trust Fund Administration, Legal Department, Treasury.
- <sup>20</sup> 1% of total fund size, divided by 12 years, and paid out of investment income.
- <sup>21</sup> Any difference between total expenses and total sources coming in FY01 will be covered by the carry-over from last fiscal year.